## APPENDIX

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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No. 17392

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MILL RIDGE COAL COMPANY,

*Appellant,*

VERSUS

GEORGE D. PATTERSON, District Director of Internal Revenue,

*Appellee.*

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*Appeal from the United States District Court for the Northern District of Alabama*

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(March 12, 1959)

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Before HUTCHESON, Chief Judge, and CAMERON and BROWN, Circuit Judges.

HUTCHESON, Chief Judge: This appeal, re-presenting here the claim for refund ineffectually urged below, that in paying the deficiency assessed against it for its fiscal year ending August 31, 1955, taxpayer overpaid its taxes, seeks a reversal of the adverse judgment. This claim was, and is, based upon taxpayer's contention that the commissioner erroneously denied it the right to deduct from its income for that year a net operating loss carry-over deduction which was based on a loss sustained by it prior to that year.

On the facts,[1] established by stipulation and undisputed testimony, the district judge, disagreeing with the reason assigned by the commissioner for the disallowance of the deduction, that it was required by Sec. 129(a) I.R.C.

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[1] Taxpayer is a Kentucky corporation organized on Sept. 18, 1947, with an authorized capital stock of 200 shares, all of which was owned by Charles and Prince DeBardeleben. The corporation operated a coal mine in Harlan County, Kentucky, and sold coal from Sept., 1948, until March, 1951.

In March, 1951, taxpayer ceased operating the mine and leased it to the Southern Kentucky Coal Company until February, 1952. From July, 1952, until September, 1952, taxpayer leased the mine to Harcrow Coals, Inc. From September, 1952, until Dec. 31, 1953, taxpayer conducted no business or operations. Taxpayer incurred a net loss during every fiscal year between August 31, 1948, and August 31, 1953.

On September 1, 1952, taxpayer sold all its physical assets, receiving in payment a secured note which it held until Dec. 31, 1953, when it was transferred to Charles and Margaret DeBardeleben. As of December 31, 1953, taxpayer's balance sheet showed zero assets and $297,140.35 worth of liabilities.

In 1949, William E. Tomlinson and R. W. Reynolds began negotiating with the Tennessee Coal and Iron Division of the United States Steel Corporation to purchase fuel oil in Baton Rouge, Louisiana, and transport it by barge and truck to TCI at Birmingham.

On Dec. 3, 1953, TCI agreed to enter such a contract. Tomlinson and Reynolds formed the Bunker Oil Company in November, 1953, through which they intended to carry out the operation. In an effort to raise capital, Tomlinson sought to sell stock to Elliott T. Williams. Williams recollected that Tomlinson approached him in October or November, 1953.

On Dec. 31, 1953, Charles and Prince DeBardeleben sold all their stock in taxpayer and taxpayer's notes, all of which they held, to Williams for $5,475.52. At that time Williams was aware of the pending contract between the Bunker Oil Company and TCI. He testified that the principal reason for buying the corporation was to get the tax benefit of its earlier losses. On Feb. 26, 1954, stock certificates in taxpayer were issued to Tomlinson, Williams, Williams' brother, James B. Morgan, and John N. Harbert III. Tomlinson testified that one of the major reasons he purchased stock in taxpayer was to obtain the tax benefit of its earlier losses.

Thereafter on March 17, 1954, TCI and taxpayer executed a formal contract providing for the transportation and sale of oil

(1939),[2] nevertheless sustained the determination of the deficiency on the ground that the reasoning of the Supreme

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by taxpayer to TCI. Taxpayer began to sell fuel oil to TCI on August 31, 1954.

Bunker Oil Company never did any business and was dissolved in 1954.

Taxpayer never engaged in any coal purchasing or selling activities after the DeBardelebens sold their stock in it.

On its income tax return for the fiscal year ended August 31, 1955, taxpayer sought to carry over and deduct the losses it had incurred in the coal business while its shares had been owned by the DeBardelebens. The District Director of Internal Revenue proposed a deficiency which taxpayer paid. Taxpayer's claim for a refund was denied, and taxpayer filed this suit. The District Court directed a verdict for the Director on the issue involved here.

[2] "Sec. 129. Acquisitions Made to Evade or Avoid Income of Excess Profits Tax.

"(a) Disallowance of Deduction, Credit, or Allowance. —If (1) any person or persons acquire, on or after October 8, 1940, directly or indirectly, control of a corporation, or (2) any corporation acquires, on or after October 8, 1940, directly or indirectly, property of another corporation, not controlled, directly or indirectly, immediately prior to such acquisition, by such acquiring corporation or its stockholders, the basis of which property, in the hands of the acquiring corporation, is determined by reference to the basis in the hands of the transferor corporation and the principal purpose for which such acquisition was made is evasion or avoidance of Federal income or excess profits tax by securing the benefit of a deduction, credit, or other allowance which such person or corporation would not otherwise enjoy, then such deduction, credit, or other allowance shall not be allowed. For the purposes of clauses (1) and (2), control means the ownership of stock possessing at least 50 per centum of the total combined voting power of all classes of stock entitled to vote or at least 50 per centum of the total value of shares of all classes of stock of the corporation.

"(b) Power of Commissioner to Allow Deduction, Etc., in Part.—In any case to which subsection (a) is applicable the Commissioner is authorized—

(1) to allow as a deduction, credit, or allowance any part of any amount disallowed by such subsection, if he determines that such allowance will not result in the evasion of avoidance

Court, in *Libson Shops, Inc.* v. *Koehler*, 353 U.S. 382, and the result in that case, required it.[3]

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of Federal income and excess profits tax for which the acquisition was made; or

(2) to distribute, apportion, or allocate gross income, and distribute, apportion, or allocate the deductions, credits, or allowances the benefit of which was sought to be secured, between or among the corporations, or properties, or parts thereof, involved, and to allow such deductions, credits, or allowances so distributed, apportioned, or allocated, but to give effect to such allowance only to such extent as he determines will not result in the evasion or avoidance of Federal income and excess profits tax for which the acquisition was made; or

(3) to exercise his powers in part under paragraph (1) and in part under paragraph (2)."

[3] Saying in that case:

"We are concerned here with a claim to carry over an operating loss to the immediately succeeding taxable year. The particular provision on which petitioner's case rests is as follows:

'If for any taxable year beginning after Dec. 31, 1947, and before Jan. 1, 1950, *the taxpayer* has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the three succeeding taxable years. . . .' (emphasis supplied) Sec. 122(b)(2)(C) 64 Stat. 937, 938, 65 Stat. 505, 26 U.S.C. Sec. 122(b)(2)(C).

"The controversy centers on the meaning of 'the taxpayer'. The contentions of the parties require us to decide whether it can be said that petitioner a combination of 16 sales businesses, is 'the taxpayer' having the pre-merger losses of three of those businesses." (p. 385)

the court, after concluding that petitioner was not "the taxpayer", went on to say:

"We do not imply that a question of tax evasion or avoidance is involved. Section 129(a) of the 1939 Code, as amended, does contain provisions which may vitiate a tax deduction that was made possible by the acquisition of corporate property for the 'principal purpose' of tax evasion or avoidance. And that section is in applicable here since there was no finding that tax evasion or avoidance was the 'principal purpose' of the merger. The fact that Sec. 129(a) is inapplicable

Taxpayer, appealing from the judgment against it, is here presenting a single question for decision. This is:

> The taxpayer corporation incurred losses while engaged in the coal mining business. The corporation disposed of all its assets and the corporate shares were then sold to new owners who engaged in the oil transportation business in the corporate name. The question is whether taxpayer is entitled to carry over the losses previously incurred, in view of the admitted principle purpose of its new shareholders in acquiring the shares to avoid taxes.

Arguing that the district judge was right in holding that Section 129(a) of the 1939 Code and its successor, Sec. 269(2) of the 1954 Code were not applicable to this case, the taxpayer citing Tax Court decisions, Northways Sec. Co., 23 B.T.A. 532; A.B. & Container Corp., 14 T.C. 842; W A G E, Inc., 19 T.C. 249; and urging upon us: that it has long been established that a single corporate taxpayer may deduct from income earned by it in one type of business in one taxable year a net operating loss sustained by it in another type of business in a prior taxable year; and that a change of business by a single corporate taxpayer does not destroy that corporation's right to carry forward its own net operating losses; insists that this rule was not changed by the decision or the opinion in the Libson case.

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does not mean that petitioner is automatically entitled to a carry-over. The availability of this privilege depends on the proper interpretation to be given to the carry-over provisions. We find nothing in those provisions which suggests that they should be construed to give a 'windfall' to a taxpayer who happens to have merged with other corporations. The purpose of these provisions is not to give a merged taxpayer a tax advantage over others who have not merged. We conclude that petitioner is not entitled to a carry-over since the income against which the offset is claimed was not produced by substantially the same businesses which incurred the losses." Libson Shops v. Koehler, 382 U.S. 382, at p. 388-9 and 390.

Calling attention to the fact that the Supreme Court, in footnote 9, 353 U.S. 390, said that it was not passing upon the instances in which a single corporate taxpayer changes its business, and assuming arguendo that that decision might apply to a single corporate taxpayer under Sec. 122(b)(2)(b) of the 1939 Code, it insists that that decision is not applicable to this case because the deduction here involved was taken by appellant in its taxable year ending 1955. Distinguishing to its own satisfaction the decision in *Coastal Oil Storage Co.* v. *Commissioner*, 242 F. (2) 396, relied on by the commissioner, on the ground that that case involved the creation of a new surtax exemption created by splitting up a profitable business and the deduction was disallowed by ignoring the separate taxable entity of the new subsidiary, appellant insists that its separate corporate taxable entity cannot be ignored here because appellant is a corporation operating an active business entirely separate and apart from its stockholders and as such has an entity and existence entirely separate and apart from them.

The United States, on its part, points as concluding the issue against appellant to the fact that the only, indeed the admitted, purpose of the purchase from the DeBardelebens of the stock of appellant, a corporation, having no assets and heavy losses, was to produce the very mischief aimed at in Sec. 129(a) I.R.C. 1939, and its successor, Sec. 269(a) of the 1954 Code, securing the tax benefits of a deduction of previous losses incurred in a different business and with different stockholders and management, against the expected great profits to be derived from the new business then being solicited by Bunker corporation for it as the heir apparent.

Pointing, too, to the fact that all of this having been arranged and confected by careful preconcert, Bunker Corporation was dissolved and the taxpayer, refurbished and reborn as Bunker's alter ego and successor, with Bunker's

stockholders and Bunker's business prospects, took over and engaged in the business, of transporting and selling oil, a business Bunker was formed to do, it insists that to permit the deduction from the expected and realized profits of the large loss carryover deduction, which was the only thing that made its acquisition by Bunker and its stockholders desirable, would be not only contrary to the construction given the carryover statute in the Libson Shops decision, *supra*, but also in the teeth of the statutes enacted to prevent this very form of tax avoidance. Emphasizing and reemphasizing that taxpayer's new stockholders had no authentic business purpose in dissolving Bunker and acquiring taxpayer through the purchase of its stock, but only the purpose of accomplishing what Sec. 129(a) of the 1939 Act and Sec. 269(a) of the 1954 Act were enacted to prevent, the abuse of loss carry-over deductions for the purpose of tax avoidance, the United States insists that the allowance of the claimed loss carry-over deduction here as a result of this neatly confected arrangement, having no business purpose and no business result, but only the purpose of avoiding taxes and achieving a tax windfall, would result in an unjust enrichment which the carry-over statute did not intend and the above referred to sections forbid.

We find ourselves in complete agreement with these views. The language and the legislative history of the enactment of the loss carry-over provisions make it quite clear that congress did not intend thereby to authorize unjust enrichments through windfalls of the kind claimed here. On the contrary, the statute, a remedial one, intended to and did provide amelioration for the drastic effects under particular circumstances of taxing income on an annual basis by allowing a business with fluctuating profits to set off its lean, against its good, years, and it cannot be reasonably contended that in enacting the carry-over provisions, congress contemplated or authorized the

trading in, and use of, the loss carry-over deduction involved here. Indeed the facts are so clear, the purpose and results of the actions taken are so obviously in conflict with the meaning and intent of the remedial statute appellant invokes that if, as we do not believe is the case, the transaction at issue here can be said to be within the letter of the statute, it is foreign to its spirit and its clearly expressed overall purpose and intent.

Agreeing with appellee, therefore, that the taxpayer here, as in the Libson case, *supra*, is not "the taxpayer" within the meaning of 26 U.S.C.A., Sec. 122(b)(2)(C); and that under the undisputed facts and the findings in this case, the allowance of the deduction is forbidden by Sec. 129(a) 1939 Code, we order the judgment

AFFIRMED.

A true copy
Test: EDWARD W. WADSWORTH
Clerk, U. S. Court of Appeals, Fifth Circuit
New Orleans, Louisiana
March 27, 1959

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**Judgment**

Extract from the Minutes of March 12, 1959.

No. 17392

MILL RIDGE COAL COMPANY,

VERSUS

GEORGE D. PATTERSON, District Director of Internal Revenue.

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District Court for the Northern District of Alabama, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

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## STATUTES INVOLVED

### Internal Revenue Code of 1939

SEC. 122. NET OPERATING LOSS DEDUCTION.

(a) Definition of Net Operating Loss.—As used in this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions, and limitations provided in subsection (d).

(b) Amount of Carry-Back and Carry-Over.—

(1) Net operating loss carry-back.—

(A) Loss for taxable year beginning before 1950.—If for any taxable year beginning after December 31, 1941, and before January 1, 1950, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the second preceding taxable year computed—

(i) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(ii) by determining the net operating loss deduction for such second preceding taxable year without regard to such net operating loss and without regard to any reduction specified in subsection (c).

(B) Loss for taxable year beginning after 1949.—If for any taxable year beginning after December 31, 1949, the

taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for the preceding taxable year.

1939 Code

(2) Net operating loss carry-over.—

(A) Loss for taxable year beginning before 1948.—Except as provided in subparagraphs (D) and (E), if for any taxable year beginning before January 1, 1948, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the two succeeding taxable years, except that the carry-over in the case of the second succeeding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the intervening taxable year computed—

(i) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(ii) by determining the net operating loss deduction for such intervening taxable year without regard to such net operating loss, without regard to any net operating loss carry-back, and without regard to any reduction specified in subsection (c).

For the purposes of the preceding sentence, the net operating loss for any taxable year beginning after December 31, 1941, shall be reduced by the sum of the net income for each of the two preceding taxable years computed—

(iii) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(iv) by determining the net operating loss deduction without regard to such net operating loss or to the net operating loss for the succeeding taxable year, and without regard to any reduction specified in subsection (c).

(B) Loss for taxable year beginning after 1949.—If for any taxable year beginning after December 31, 1949, the

taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the five succeeding taxable years, except that the carry-over in the case of each such succeeding taxable year (other than the first succeeding taxable year) shall be the excess, if any, of the amount of such net operating loss over the sum of the net income for each of the intervening years computed—

(i) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(ii) by determining the net operating loss deduction for each intervening taxable year, without regard to such net operating loss or to the net operating loss for any succeeding taxable year and without regard to any reduction specified in subsection (c).

For the purpose of the preceding sentence, the net operating loss for any taxable year beginning after December 31, 1949, shall be reduced by the amount, if any, of the net income for the preceding taxable year computed—

(i) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(ii) by determining the net operating loss deduction for such preceding taxable year without regard to such net operating loss and without regard to any reduction specified in subsection (c).

(C) Loss for taxable year beginning after December 31, 1947, and before January 1, 1950.—If for any taxable year beginning after December 31, 1947, and before January 1, 1950, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the three succeeding taxable years, except that the carry-over in the case of each such succeeding taxable year (other than the first succeeding taxable year) shall

be the excess, if any, of the amount of such net operating loss over the sum of the net income for each of the intervening years computed—

(i) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(ii) by determining the net operating loss deduction for each intervening taxable year without regard to such net 1939 Code
operating loss or to the net operating loss for any succeeding taxable year and without regard to any reduction specified in subsection (c).

For the purpose of the preceding sentence, the net operating loss for any taxable year beginning after December 31, 1947, and before January 1, 1950, shall be reduced by the sum of the net income for each of the two preceding taxable years computed—

(iii) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and

(iv) by determining the net operating loss deduction without regard to such net operating loss or to the net operating loss for the succeeding taxable year, and without regard to any reduction specified in subsection (c).

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(c) Amount of Net Operating Loss Deduction.—The amount of the net operating loss deduction shall be the aggregate of the net operating loss carry-overs and of the net operating loss carry-backs to the taxable year reduced by the amount, if any, by which the net income (computed with the exceptions and limitations provided in subsection (d) (1), (2), (3), and (4)) exceeds, in the case of a taxpayer other than a corporation, the net income (computed without such deduction), or, in the case of a corporation, the normal-tax net income (computed without such deduction and without the credit provided in section 26 (h) and (i)).

(d) Exceptions, Additions, and Limitations.—The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

(1) The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value or to percentage depletion under section 114 (b) (2), (3), or (4);

(2) There shall be included in computing gross income the amount of interest received which is wholly exempt from the taxes imposed by this chapter, decreased by the amount of interest paid or accrued which is not allowed as a deduction by section 23 (b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations;

(3) No net operating loss deduction shall be allowed;

(4) The amount deductible on account of losses from sales or exchanges of capital assets shall not exceed the amount includible on account of gains from such sales or exchanges. The deduction provided in section 23 (ee) shall not be allowed.

(5) Deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer shall (in the case of a taxpayer other than a corporation) be allowed only to the extent of the amount of the gross income not derived from such trade or business. For the purposes of this paragraph, deductions and gross income shall be computed with the exceptions, additions, and limitations specified in paragraphs (1) to (4) of this subsection. This paragraph shall not apply with respect to deductions allowable for losses sustained after December 31, 1950, in respect to property, if the losses arise from fire, storm, shipwreck, or other casualty, or from theft.

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(c) No Carry-Back to Year Prior to 1941.—As used in this section, the term "preceding taxable year" and the term "preceding taxable years" do not include any taxable year beginning prior to January 1, 1941.

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SEC. 129. ACQUISITIONS MADE TO EVADE OR AVOID INCOME OR EXCESS PROFITS TAX.

(a) Disallowance of Deduction, Credit, or Allowance.—If (1) any person or persons acquire, on or after October 8, 1940, directly or indirectly, control of a corporation, or (2) any corporation acquires, on or after October 8, 1940, directly or indirectly, property of another corporation, not controlled, directly or indirectly, immediately prior to such acquisition, by such acquiring corporation or its stockholders, the basis of which property, in the hands of the acquiring corporation, is determined by reference to the basis in the hands of the transferor corporation and the principal purpose for which such acquisition was made is evasion or avoidance of Federal income or excess profits tax by securing the benefit of a deduction, credit, or other allowance which such person or corporation would not otherwise enjoy, then such deduction, credit, or other allowance shall not be allowed. For the purposes of clauses (1) and (2), control means the ownership of stock possessing at least 50 per centum of the total combined voting power of all classes of stock entitled to vote or at least 50 per centum of the total value of shares of all classes of stock of the corporation.

(b) Power of Commissioner to Allow Deductions, Etc., in Part.—In any case to which subsection (a) is applicable the Commissioner is authorized—

(1) to allow as a deduction, credit, or allowance any part of any amount disallowed by such subsection, if he determines that such allowance will not result in the evasion or avoidance of Federal income and excess profits tax for which the acquisition was made; or

(2) to distribute, apportion, or allocate gross income, and distribute, apportion, or allocate the deductions, credits, or allowances the benefit of which was sought to be secured, between or among the corporations, or properties, or parts thereof, involved, and to allow such deductions, credits, or allowances so distributed, apportioned, or allocated, but to give effect to such allowance only to such extent as he determines will not result in the evasion or avoidance of Federal income and excess profits tax for which the acquisition was made; or

(3) to exercise his powers in part under paragraph (1) and in part under paragraph (2).

1954 Code

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**Internal Revenue Code of 1954**

SEC. 172. NET OPERATING LOSS DEDUCTION.

(a) Deduction Allowed—There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term "net operating loss deduction" means the deduction allowed by this subsection.

(b) Net Operating Loss Carrybacks and Carryovers.—

(1) Years to which loss may be carried.—A net operating loss for any taxable year ending after December 31, 1957, shall be—

(A) a net operating loss carryback to each of the 3 taxable years preceding the taxable year of such loss, and

(B) a net operating loss carryover to each of the 5 taxable years following the taxable year of such loss.

(2) Amount of carrybacks and carryovers.—Except as provided in subsection (i), the entire amount of the net operating loss for any taxable year (hereinafter in this

section referred to as the 'loss year'), shall be carried to the earliest of the 8 taxable years to which (by reason of subparagraphs (A) and (B) of paragraph (1)) such loss may be carried. The portion of such loss which shall be carried to each of the other 7 taxable years shall be the excess, if any, of the amount of such loss over the sum of the taxable income for each of the prior taxable years to which such loss may be carried. For purposes of the preceding sentence, the taxable income for any such prior taxable year shall be computed—

(A) with the modifications specified in subsection (d) other than paragraphs (1), (4), and (6) thereof; and

(B) by determining the amount of the net operating loss deduction without regard to the net operating loss for the loss year or for any taxable year thereafter, and the taxable income so computed shall not be considered to be less than zero.

(c) Net Operating Loss Defined.—For purposes of this section, the term "net operating loss" means (for any taxable year ending after December 31, 1953) the excess of the deductions allowed by this chapter over the gross income. Such excess shall be computed with the modifications specified in subsection (d).

(d) Modifications.—The modifications referred to in this section are as follows:

(1) Net operating loss deductions.—No net operating loss deduction shall be allowed.

(2) Capital gains and losses of taxpayers other than corporations.—In the case of a taxpayer other than a corporation—

(A) the amount deductible on account of losses from sales or exchanges of capital assets shall not exceed the

amount includible on account of gains from sales or exchanges of capital assets; and

(B) the deduction for long-term capital gains provided by section 1202 shall not be allowed.

(3) Deduction for personal exemptions.—No deduction shall be allowed under section 151 (relating to personal exemptions). No deduction in lieu of any such deduction shall be allowed.

(4) Nonbusiness deductions of taxpayers others than corporations.—In the case of a taxpayer other than a corporation, the deductions allowable by this chapter which are not attributable to a taxpayer's trade or business shall be allowed only to the extent of the amount of the gross income not derived from such trade or business. For purposes of the preceding sentence—

(A) any gain or loss from the sale or other disposition of—

(i) property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 167, or

(ii) real property used in the trade or business, shall be treated as attributable to the trade or business;

(B) the modifications specified in paragraphs (1), (2) (B), and (3), shall be taken into account; and

(C) any deduction allowable under section 165 (c) (3) (relating to casualty losses) shall not be taken into account.

(5) Special deductions for corporations.—No deduction shall be allowed under section 242 (relating to partially tax-exempt interest) or under section 922 (relating to Western Hemisphere trade corporations).

(6) Computation of deduction for dividends received, etc.—The deductions allowed by sections 243 relating to dividends received by corporations), 244 (relating to dividends received on certain preferred stock of public utilities), and 245 (relating to dividends received from certain foreign corporations) shall be computed without regard to section 246(b) (relating to limitation on aggregate amount of deductions); and the deduction allowed by section 247 (relating to dividends paid on certain preferred stock of public utilities) shall be computed without regard to subsection (a) (1) (B) of such section.

(e) Law Applicable to Computations.—In determining the amount of any net operating loss carryback or carryover to any taxable year, the necessary computations involving any other taxable year shall be made under the law applicable to such other taxable year. The preceding sentence shall apply with respect to all taxable years, whether they begin before, on, or after January 1, 1954.

(f) Taxable Years Beginning in 1953 and Ending in 1954.—In the case of a taxable year beginning in 1953 and ending in 1954—

(1) In lieu of the amount specified in subsection (c), the net operating loss for such year shall be the sum of—

(A) that portion of the net operating loss for such year computed without regard to this subsection which the number of days in the loss year after December 31, 1953, bears to the total number of days in such year, and

(B) that portion of the net operating loss for such year computed under section 122 of the Internal Revenue Code of 1939 as if this section had not been enacted which the number of days in the loss year before January 1, 1954, bears to the total number of days in such year.

(2) The amount of any net operating loss for such year which shall be carried to the second preceding taxable

year is the amount which bears the same ratio to such net operating loss as the number of days in the loss year after December 31, 1953, bears to the total number of days in such year. In determining the amount carried to any other taxable year, the reduction for the second taxable year preceding the loss year shall not exceed the portion of the net operating loss which is carried to the second preceding taxable year.

(3) The net operating loss deduction for such year shall be, in lein of the amount specified in section 122 (c) of the Internal Revenue Code of 1939, the sum of—

(A) that portion of the net operaitng loss deduction for such year, computed as if subsection (a) of this section were applicable to the taxable year, which the number of days in such year after December 31, 1953, bears to the total number of days in such year, and

(B) that portion of the net operating loss deduction for such year, computed under section 122 (c) of the Internal Revenue Code of 1939 as if this paragraph had not been enacted, which the number of days in such year before January 1, 1954, bears to the total number of days in such year.

(4) For purposes of the second sentence of subsection (b) (2), the taxable income for such year shall be the sum of—

(A) that portion of the net income for such year, computed without regard to this paragraph, which the number of days in such year before January 1, 1954, bears to the total number of days in such year, and

(B) that portion of the net income for such year, computed—

(i) without regard to paragraphs (1) and (2) of section 122 (d) of the Internal Revenue Code of 1939, and

(ii) by allowing as a deduction an amount equal to the sum of the credits provided in subsections (b) and (h) of section 26 of such Code,

which the number of days in such year after December 31, 1953, bears to the total number of days in such year.

(g) Special Transitional Rules.—

(1) Losses for taxable years ending before January 1, 1954.—For purposes of this section, the determination of the taxable years ending after December 31, 1953, to which a net operating loss for any taxable year ending before January 1, 1954, may be carried shall be made under the Internal Revenue Code of 1939.

(2) Losses for taxable years ending after December 31, 1953.—For purposes of section 122 of the Internal Revenue Code of 1939—

(A) the determination of the taxable years ending before January 1, 1954, to which a net operating loss for any taxable year ending after December 31, 1953, may be carried shall be made under subsection (b) (1) (A) of this section; and

(B) in determining the amount of the carryback to the first taxable year preceding the first taxable year ending after December 31, 1953, the portion of the net operating loss carried to such year shall be such net operating loss reduced by—

(i) the net income for the second preceding taxable year, computed as if the second sentence of section 122 (b) (2) (B) of the Internal Revenue Code of 1939 applied, or

(ii) if smaller, the portion of the net operating loss which by reason of subsection (f) of this section is carried to the second preceding taxable year.

(3) Taxable years beginning after December 31, 1953, and ending before August 17, 1954.—In the case of a tax-

able year which begins after December 31, 1953, and ends before August 17, 1954—

(A) the net operating loss deduction for such year shall be computed as if subsection (a) of this section applied to such taxable year, and

(B) for purposes of the second sentence of subsection (b) (2), the taxable income for such taxable year shall be the net income for such taxable year, computed—

(i) without regard to paragraphs (1) and (2) of section 122 (d) of the Internal Revenue Code of 1939, and

(ii) by allowing as a deduction an amount equal to the sum of the credits provided in subsections (b) and (h) of section 26 of such Code.

(4) Excess profits tax not affected.—For purposes of subchapter D of chapter 1 of the Internal Revenue Code of 1939, excess profits net income shall be computed as if this section had not been enacted and as if section 122 of such Code continued to apply to taxable years to which this substitute applies.

(h) Disallowance of Net Operating Loss of Electing Small Business Corporations.—In determining the amount of the net operating loss deduction under subsection (a) of any corporation, there shall be disregarded the net operating loss of such corporation for any taxable year for which such corporation is an electing small business corporation under subchapter S.

(i) Carryback of Net Operating Loss for Taxable Years Beginning in 1957 and Ending in 1958.—In the case of a table year beginning in 1957 and ending in 1958, the amount of any net operating loss for such year which shall be carried to the third preceding taxable year is the amount which bears the same ratio to such net operating

loss as the number of days in the loss year after December 31, 1957, bears to the total number of days in such year. In determining the amount carried to any other taxable year, the reduction for the third taxable year preceding the loss year shall ont exceed the portion of the net operating loss which is carried to the third preceding taxable year.

(j) Cross References.—

(1) For treatment of net operating loss carryovers in certain corporate acquisitions, see section 381.

(2) For special limitation on net operating loss carryovers in case of a corporate change of ownershiu, see section 382.

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SEC. 269. ACQUISITIONS MADE TO EVADE OR AVOID INCOME TAX.

(a) In General.—If—

(1) any person or persons acquire, or acquired on or after October 8, 1940, directly or indirectly, control of a corporation, or

(2) any corporation acquires, or acquired on or after October 8, 1940, directly or indirectly, property of another corporation, not controlled, directly or indirectly, immediately before such acquisition, by such acquiring corporation or its stockholders, the basis of which property, in the hands of the acquiring corporation, is determined by reference to the basis in the hands of the transferor corporation,

and the principal purpose for which such acquisition was made is evasion or avoidance of Federal income tax by securing the benefit of a deduction, credit, or other allowance which such person or corporation would not otherwise enjoy, then such deduction, credit, or other allowance

shall not be allowed. For purposes of paragraphs (1) and (2), control means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote or at least 50 percent of the total value of shares of all classes of stock of the corporation.

(b) Power of Secretary or His Delegate to Allow Deduction, etc., in Part.—In any case to which subsection (a) applies, the Secretary or his delegate is authorized—

(1) to allow as a deduction, credit, or allowance any part of any amount disallowed by such subsection, if he determines that such allowance will not result in the evasion or avoidance of Federal income tax for which the acquisition was made; or

(2) to distribute, apportion, or allocate gross income, and distribute, apportion, or allocate the deductions, credits, or allowances the benefit of which was sought to be secured, between or among the corporations, or properties, or parts thereof, involved, and to allow such deductions, credits, or allowances so distributed, appointed, or allocated, but to give effect to such allowance only to such extent as he determines will not result in the evasion or avoidance of Federal income tax for which the acquisition was made; or

(3) to exercise his powers in part under paragraphs (1) and in part under paragraph (2).

(c) Presumption in Case of Disproportionate Purchase Price.—The fact that the consideration paid upon an acquisition by any person or corporation described in subsection (a) is substantially disproportionate to the aggregate—

(1) of the adjusted basis of the property of the corporation (to the extent attributable to the interest acquired specified in paragraph (1) of subsection (a)), or of the

property acquired specified in paragraph (2) of subsection (a); and

(2) of the tax benefits (to the extent not reflected in the adjusted basis of the property) not available to such person or corporation otherwise than as a result of such acquisition,

shall be prima facie evidence of the principal purpose of evasion or avoidance of the Federal income tax. This subsection shall apply only with respect to acquisitions after March 1, 1954.